

# **THE PUBLIC SCHOOL BENEFITS OF EDUCATION SAVINGS ACCOUNTS**

## **THE IMPACT OF ESAs IN ARIZONA**

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## Introduction & Executive Summary

They've been praised as a lifeline for students in need, derided as a harm to America's unionized education establishment, and debated vigorously in state legislatures across the country.<sup>1</sup>

Known commonly as education savings accounts (ESAs), they are now accessed by thousands of families in the state of Arizona, while in 2017, activists gathered thousands of signatures and successfully campaigned against making them available to all students in the state. In 2019, Tennessee legislators expanded them to low-income pupils, while in West Virginia, union leaders organized a teacher strike to prevent them and other school choice measures from even taking shape.<sup>2</sup>

Yet amid the enthusiasm and emotions for and against ESAs, few have a thorough understanding of their overall impact beyond a handful of competing claims such as “they give families a choice in education” or “they hurt public schools.” This report offers a uniquely detailed account of their impact on families, schools, and state taxpayers in the country's most developed education savings account model, Arizona's Empowerment Scholarship Account program.

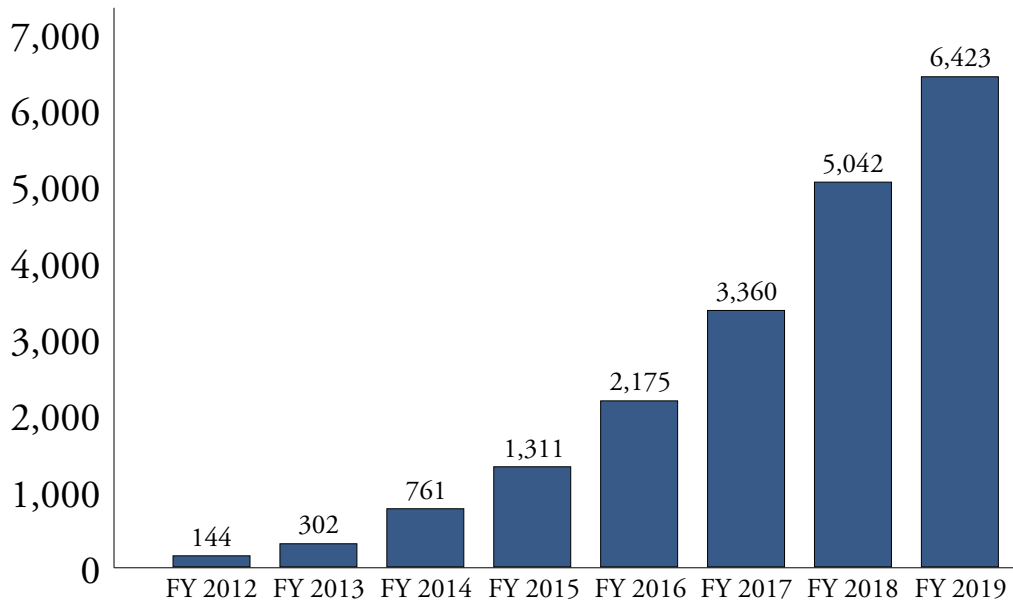
Among the report's key findings:

- ❑ ESAs served over 6,400 students in Arizona in FY 2019, including over 3,700 with special needs and more than 800 whose families serve in the armed forces or have fallen in the line of duty.
- ❑ ESAs complement existing public school choice options: District schools are 15 times likelier to “lose” a student through competition with another public school than to an ESA, among eligible populations.
- ❑ ESA families received an average award of \$6,148 for non-special needs students in FY 2019, re-

quiring substantially less in taxpayer funding than Arizona's \$10,120 public school average per pupil spending the same year.

- ❑ Arizona's FY 2020 budget directs \$3 million of ESA savings to overhaul the state's IT system used to calculate the payments to every single public school in the state, benefitting over 1.1 million public school students.
- ❑ ESAs *increase per pupil public school spending* by redistributing state and federal dollars back to remaining public school students. From state sources alone, ESAs redirect over \$600 per participant back to remaining public school students for teacher pay and other operational uses.
- ❑ ESAs ease the costs of enrollment growth and school construction in Arizona's public school system, which currently increases state taxpayer costs by over \$180 million per year, limiting the funding that is available to increase *per pupil* expenditures.<sup>3</sup>
- ❑ ESAs often *reduce budget pressures* on public schools by serving students with severe disabilities, one of the most high-need, high-cost populations, whom districts state they can serve only by redirecting funds from other students' instruction.
- ❑ Despite headlines to the contrary, Arizona's ESA program has proven remarkably effective in deploying public funds toward children's educational needs: Roughly 99 percent of ESA monies are used as intended, with alleged program mis-spending often involving educational purchases previously approved by the Arizona Department of Education.

## Arizona Empowerment Scholarship Account Program Participation



Source: ESA FY 2019 program data provided by the Arizona Department of Education, April 23, 2019. Historical enrollment data from Arizona Joint Legislative Budget Committee FY 2020 Baseline. FY 2019 participation totals reflect all students served by the ESA program at any point in FY 2019.

### Arizona: Birthplace of the ESA Program

Pioneered by the Goldwater Institute and first enacted in Arizona in 2011, education savings account programs provide families with resources to pursue educational avenues that fit their children’s needs while helping to relieve spending by taxpayers.<sup>4</sup> Specifically, Arizona’s ESAs—known as Empowerment Scholarship Accounts—take a portion of what the state would have spent covering the cost of a student’s education in a public school and instead deposit that money into a personalized account that allows the child’s family to use the funds for tutoring, educational therapies, private school tuition, curriculum materials, and other teaching tools.<sup>5</sup>

ESAs now offer such opportunities to families across the country, with North Carolina becoming the

sixth state to enact an ESA program beginning in the 2018-2019 school year.<sup>6</sup>

In Arizona, ESA eligibility has gradually expanded to serve several student populations, including some of the state’s most disadvantaged children. As of 2019, program eligibility encompasses the following<sup>7</sup>:

- Students with special needs
- Students from Native American reservations
- Foster care students
- Students from public schools rated D or F by the State Board of Education
- Prior ESA participants and siblings
- Children of active duty or fallen members of the armed services

As the program has become accessible to more of these groups over time, the number of participating students has grown from 144 students during its first year of implementation in Fiscal Year 2012 to 6,423 students in Fiscal Year 2019.<sup>8</sup>

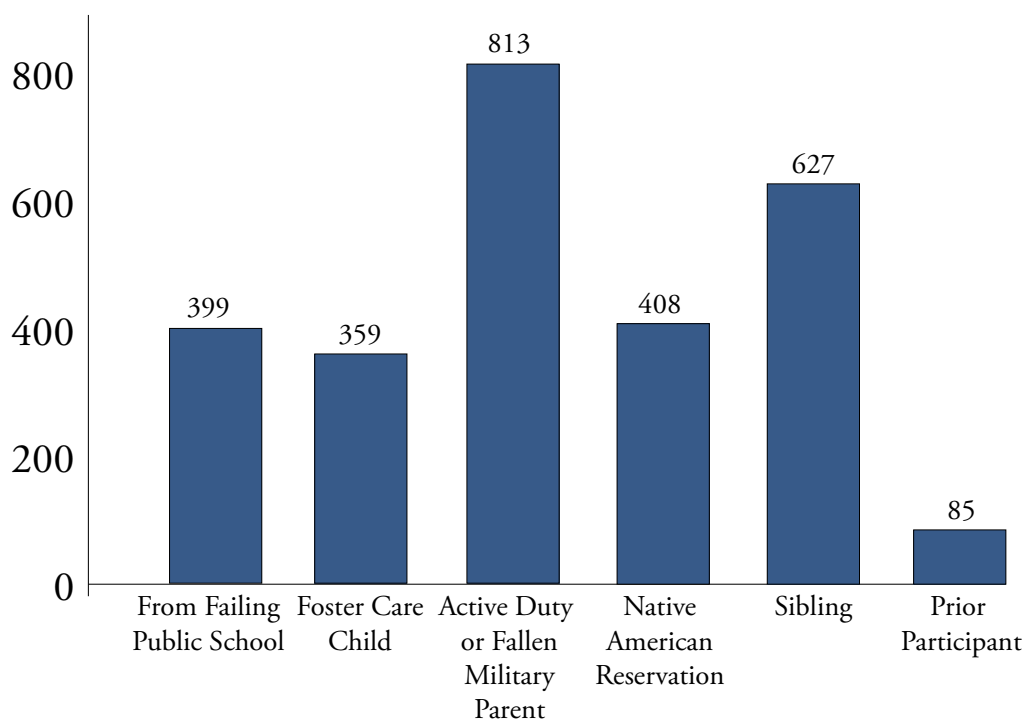
### Arizona's ESA Program: Serving Those in Need, Those Who Serve

Children with special needs have benefitted from the ESA program more than any other student group to date. These pupils accounted for 3,732, or 58 percent, of Arizona's ESA participants in FY 2019, while the remaining categories together comprised 2,691 participants, or 42 percent.

Children of active duty or fallen members of the armed services have benefitted from the ESA program in the greatest numbers among non-special needs participants, with 813 using the program in FY 2019. Throughout the state, 408 students from Native American reservations also benefitted from the program in FY 2019, as did 399 students coming from failing public schools and 359 students from the foster care system.

The ESA program also served an additional 627 students who were eligible as participants' siblings, and 85 students who were eligible as previous participants. (Siblings and prior participants may also qualify under the other eligibility criteria, but the Arizona Department of Education [ADE] data does not report when a student meets multiple criteria.)

### ESA Beneficiaries: FY 2019 Non-Special Needs Participants, by Eligibility



Source: ESA FY 2019 program data provided by the Arizona Department of Education, April 23, 2019.

\*While students may meet more than one eligibility criteria, only one criterion is recorded in the official program data for each participant. As a result, the actual number of students qualifying under each category may be higher. Students labeled as "prior participants" qualified under other criteria originally.

Among ESA participants with special needs, over two-thirds are children with significant disabilities. These students include those with severe intellectual disabilities, visual impairments, hearing impairments, and other conditions, and they generate substantially more funding than non-special needs students under Arizona’s school funding formula (described below).

The remaining third of special needs ESA participants comprise students with more mild conditions, including developmental delays, mild intellectual disabilities, and speech and language impairments.

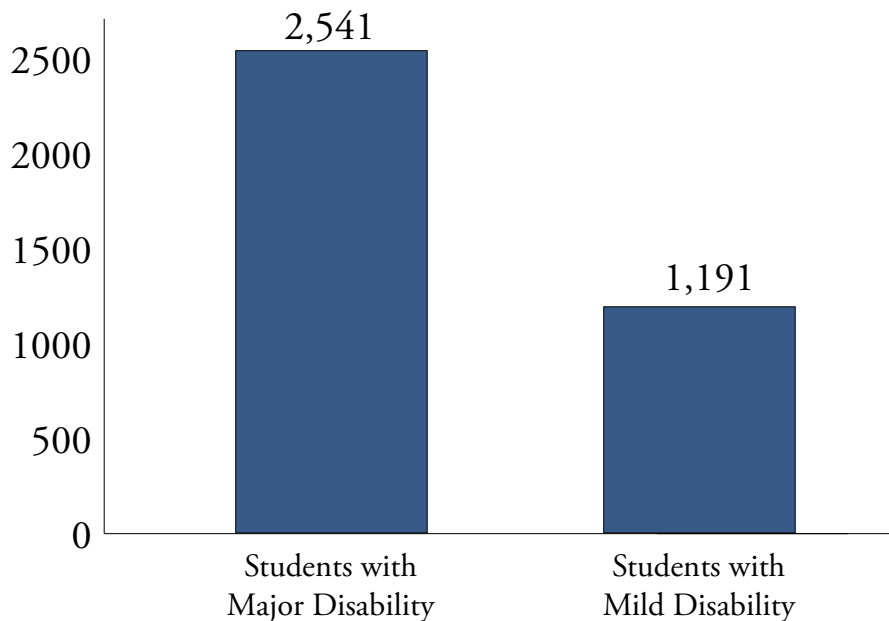
### Taxpayer Savings from ESAs

As in many states, funding for Arizona’s public K-12 schools comes from a variety of local, state, and federal sources including property, income, and sales

tax revenues, the state’s Land Trust endowment fund, and charitable donations. Taken together, these funding sources provide an estimated \$10,120 per pupil as of FY 2019,<sup>9</sup> and for students with special needs, the total can exceed \$30,000 per student.

These taxpayer resources are no longer expended on a child who opts out of public school and into Arizona’s ESA program, however. Instead, part of the state-funded portion is deposited into the family’s ESA account based on a statutorily prescribed formula. That ESA formula amount equals 90 percent of the funding that would have been generated by the “base support level” and “additional assistance” amounts (two of the basic components of Arizona’s public school student funding formula).

## ESA Beneficiaries FY 2019 Special Needs Participants

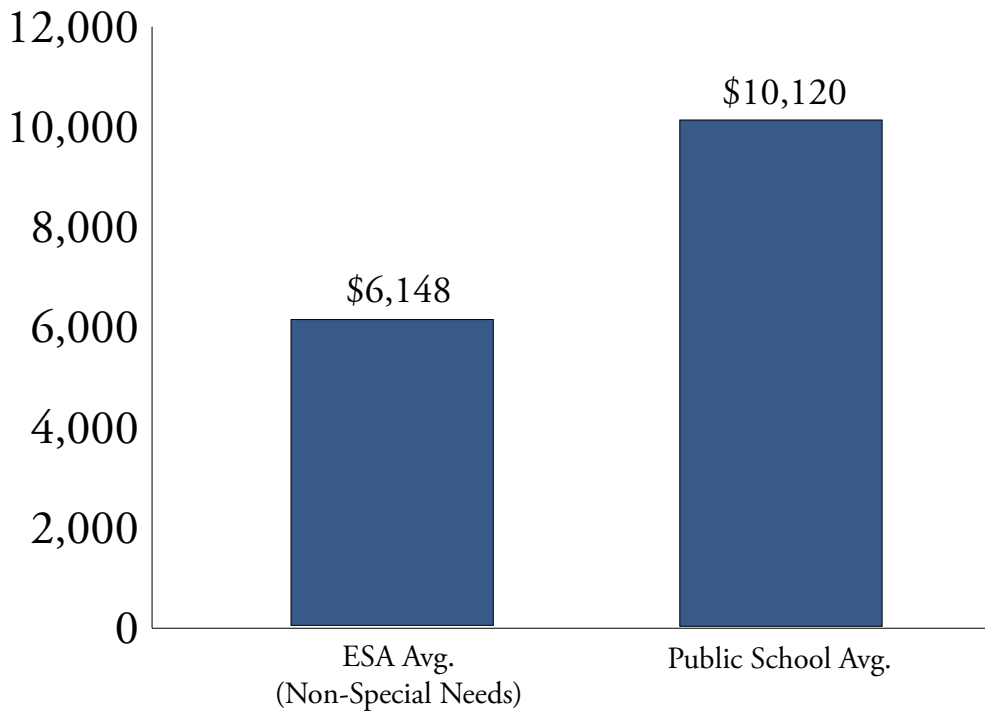


Source: ESA FY 2019 program data provided by the Arizona Department of Education, April 23, 2019.

Students designated as having major disabilities include those who receive funding multipliers greater than 1.0 in the state’s “Group B” weighting formula. Conditions include severe sensory impairment, orthopedic impairment, moderate or severe intellectual disabilities, emotional disabilities, visual or hearing impairments, and preschool severe delay diagnoses.

Students designated as having more mild disabilities would receive nominal additional funding under the regular state funding formula equivalent to a multiplier of 0.003. Conditions include developmental delay, emotional disability, mild intellectual disability, specific learning disability, and speech and language impairments.

## ESA vs. Public School Per Pupil Costs in Arizona, FY 2019



Source: ESA FY 2019 program data provided by the Arizona Department of Education, April 23, 2019. FY 2019 public school average as reported by Arizona Joint Legislative Budget Committee. ESA award amounts exclude 5% administrative set-aside to ADE and the State Treasurer, which totals approximately \$300 per participant.

However, the ESA formula amount does not provide any portion of the funding that would have been spent on a public school student from other funding sources, including the state's Classroom Site Fund, the transportation reimbursement formula, federal funding, locally approved property tax increases, and facilities funding.

As a result, ESA award amounts for (non-kindergarten) non-special needs participants averaged \$6,148 as of FY 2019, far less than the \$10,120 per pupil costs officially estimated by the state's legislative budget office for an Arizona public school student in FY 2019.<sup>10</sup> (The latter amount is slightly elevated by additional funding generated by high-cost special needs students, which is included in the overall public school average. However, even excluding the

additional state and federal funds associated with these students, the statewide public school per pupil spending would remain over \$9,500 per student, still well above the funding for a comparable ESA participant—as discussed below.)

Among special needs students, ESA families received an average of \$19,989 in FY 2019. (Students with major disabilities received \$26,707 on average, while ESA grade-schoolers with mild disabilities received \$6,173 on average).<sup>11</sup> In each of these cases, the ESA amounts represent a smaller cost than would have been spent on the students in a public school setting.

While the ESA program thus serves thousands of disadvantaged students—at an overall savings to taxpayers—opponents of school choice have aggressively targeted it, seeking to restrict or eliminate the op-



portunities ESAs offer students outside of traditional public education.<sup>12</sup>

The following sections address many of the chief arguments put forward *against* the ESA program.

### **Claim: ESAs Undermine Public Education**

*“None of our recent re-investments in teacher pay or school funding will matter if we let [ESA expansion] drain millions of dollars every year.”*

— Save Our Schools Arizona<sup>13</sup>

Perhaps the most serious charge leveled against ESAs is the assertion they threaten public education by diverting necessary resources from already underfunded public schools.

Critics of the ESA program often make this claim as one of two mutually incompatible arguments against ESAs. Specifically, critics assert that 1) only affluent families who can already afford private school will use ESAs, but that 2) ESAs will lead to a dramatic exodus of students (and the dollars that follow them) from their local public schools.

If the first claim is true—meaning that ESAs merely subsidize families who can already afford private education—then ESAs should have a negligible impact on the enrollment figures of public schools since those wealthy families would have enrolled in private school anyway if they so desired.

Clearly, ESA critics cannot have it both ways: At least one of the claims must be false. Available evidence suggests that both assertions are off base.

### **Reality: ESAs Serve Families *Without Disruption* to Public School Enrollment**

The argument that ESAs threaten to siphon off vast numbers of students and thus drain school districts of pupils and funding stands at odds with the program’s

already observable participation data. Looking at the largest group of ESA-eligible students in particular—those with special needs—only 2.9 percent participated in the program as of FY 2019.<sup>14</sup> Prior estimates have likewise found that fewer than 3 percent of all students eligible for the ESA program have availed themselves of it.<sup>15</sup>

In comparison, 18 percent of public school students statewide have opted to attend a charter rather than district school as of FY 2019.<sup>16</sup> Yet even this much larger impact from charter schools is dwarfed by the share of students leaving their local district schools for *other district schools*.

For example, a recent analysis of sampled school districts in Maricopa County (which contains the Phoenix metropolitan area) found that over 30 percent of public school students had taken advantage of the state’s “open enrollment” process to attend a district school other than the one they were assigned to by their zip code.<sup>17</sup> Combined with those attending charter schools, that means nearly half (47 percent) of public school students were attending a school other than the one they would have been assigned to by their zip code.

In other words, a 3 percent participation rate in the ESA program would amount to a mere sliver of the overall K-12 landscape, and the proportion of students opting out of their local district school for *existing* alternatives is more than 15 times larger than the comparable impact of ESAs.

Some might respond that, rather than allowing families continued access to educational opportunities outside their assigned district campus, charters and other choice options should be curtailed or eliminated. This would seem a poor solution for the hundreds of thousands of families who’ve found these avenues more fully meet their children’s needs.

## Reality: ESAs Increase Funding Available to School Districts

Most public school advocates agree that *per pupil* funding—rather than *total* funding—is the more important barometer of our investments in K-12 education. This is why, even though total K-12 spending in Arizona has increased since 2001 by more than \$5 billion (or 34 percent, adjusted for inflation), organizations like the Children’s Action Alliance have alleged that Arizona has *cut* funding for public schools.<sup>18</sup>

Total funding may have increased by billions of dollars, the argument goes, but because there are so many more students to educate today than in 2001, Arizona’s current *per pupil* amounts reflect unacceptable decreases in education spending. (In reality, while Arizona’s inflation adjusted per pupil spending remains below its 2008 peak, it is actually slightly higher than it was in 2001.<sup>19</sup>)

Yet when it comes to ESAs, many of these same advocates abandon their fidelity to per pupil measurements of education spending. This is because ESAs actually *increase* the resources available to public school students on a per pupil basis.

Generally speaking, Arizona’s school funding formula injects more money into public education when more students are enrolled. Likewise, if a district or charter’s enrollment declines, they no longer receive the funding for those students whom they no longer educate.

However, Arizona’s public schools actually retain a significant portion of a student’s funding even if that student exits the system for an ESA. This is because several pieces of Arizona’s school funding formula are based on fixed pools of money, which do not decrease as students exit the public school system. Rather, the same amount of money is simply spread out among

fewer students, meaning that each remaining student receives a greater amount.

## ESAs Increase Per Pupil State and Local Funding for Public Schools

For example, Arizona’s Classroom Site Fund (CSF), which provided \$579 million for teacher pay, classroom size reduction, etc. in FY 2019, is funded by available state sales tax and State Land Trust revenues, independent of the number of students in public schools.<sup>20</sup> The total pool of CSF money is simply divided among the 1.1 million public school students in the state, which translates to about \$532 per student. So for every single pupil who leaves the public school system for an ESA, \$532 is returned to the pot.

The CSF is just one of several fixed pools of money that concentrate more resources on remaining public school students each time an ESA participant exits public school. The Instructional Improvement Fund from tribal gaming revenues (\$45 million) and supplemental funding from Proposition 123 (\$50 million) are likewise fixed amounts distributed evenly among all remaining public school students.<sup>21</sup>





Additional funding sources such as tax credit donations to public schools for extracurricular activities (\$57 million<sup>22</sup>) similarly remain available for existing public school students as other pupils opt for the ESA program.

From these sources of funding alone, the ESA program redirects an average of \$654 *per participant* back to public schools to be redistributed among the remaining pupils.

This means the 6,423 ESA participants are redirecting over \$4.2 million per year in education dollars back to other public school pupils.

## ESAs Redirect Federal Funds to Low-Income Public School Students

But that is not all. Arizona receives over \$1.1 billion of federal money to support K-12 students in Arizona each year<sup>23</sup> (more than \$1,000 per pupil), and a substantial portion of this money also stays in the public school system even as students exit for alternatives like ESAs. For example, the approximately \$350 million of federal Title I-A grants directed to Arizona each year—which are intended to support the education of children from low-income families—provide a higher per pupil benefit to public schools as more students participate in alternatives like the ESA program.

This is because Title I funds are allocated to school districts based on the number of school-aged children living in poverty within each district's geographic area (as measured by U.S. census data) rather than on the number of students who actually *attend* district-operated campuses.<sup>24</sup> (Federal law directs districts to equitably share Title I resources with private schools, but as researchers at New America have observed, “While there is a fair amount of federal money available to private schools, particularly those serv-

ing low-income children, not all private schools take advantage of these federal funds” because “federal money comes with a lot of federal requirements” and private schools often “don't have the administrative capacity to [negotiate and set up arrangements with the district].”<sup>25</sup>)

Federal funds thus do not necessarily follow low-income students who transfer out of a public school to a private one or to a homeschooling arrangement. This leaves more resources available for the remaining public school students.

Moreover, ESAs help redirect Title I monies back toward low-income public school students when higher-income students exit the public school system as well. This is because federal law allows most schools to spend their Title I funds on all students—not just the low-income students the program is intended to serve. This has led to a situation in which, according to the U.S. Department of Education, “about 11.6 million children are counted as formula eligible [for Title I assistance based on their income], while about 25.0 million students in the United States receive Title I services.”<sup>26</sup>

In other words, more than half of Title I beneficiaries are not even the program's intended recipients, leaving the Brookings Institution to observe that “Title I is spread so thin that its budget of \$14 billion a year [nationally] turns out not to be much money.”<sup>27</sup> Like Arizona's Classroom Site Fund, the available pot of federal money has been stretched into smaller per pupil amounts to cover a larger K-12 population, when it could instead be concentrated into higher per pupil support for its intended beneficiaries if it were focused more exclusively upon them. ESAs help achieve this result.

## ESAs Help When ‘Just Add More Money’ Does Not

One common retort is that policymakers should simply increase the amount of funding going into these pools of money rather than allow alternative pathways like ESAs. However, pouring in more money is essentially the very same approach Arizona has taken over the last several decades in an attempt to keep up with surging K-12 enrollments.

As the Arizona Tax Research Association (ATRA) has reported, for example, “Since the Census Bureau began tracking [school] spending, Arizona has consistently ranked in the top 10 states who increased dollars to their entire K-12 education system,” yet this reliable increase in K-12 spending overall has failed to translate into *per pupil* increases because Arizona has also consistently needed to use those K-12 dollars just to pay for the growing number of students in its schools. This is no coincidence, since as ATRA observes more broadly, “most of the states who occupy the bottom of per pupil spending are the states who grew the most . . . The reverse is also highly correlative: states in the bottom of K-12 student growth find themselves near the top of per pupil spending.”<sup>28</sup>

To illustrate this in more concrete terms, Arizona spent an additional \$84 million in FY 2019 simply to absorb the costs of more students enrolling in the public school system.<sup>29</sup> This amount was on top of an \$88 million increase the year before that, which was itself layered on top of a \$74 million increase the year before that, and so forth.<sup>30</sup> These increases compound into hundreds of millions of dollars of additional funding each year, yet they are generally waived off by pundits because they do not increase *per pupil* public school spending. If Arizona’s K-12 enrollment growth were flatter, however, each of these annual increases could instead be used to significantly boost Arizona’s per pupil funding.

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None of this is to say that increases in student enrollment should be discouraged, but policymakers and the public often fail to appreciate the enormous impact that enrollment costs play in determining available funding *per student*. This is especially true in debates over the ESA program, where critics allege that ESAs take money away from public schools, while papering over the fact that the ESA program leaves the public school system shouldering the expense of fewer students.

## ESA Savings Are Now Being Used to Fund Public School IT Needs

Beyond the various indirect benefits of the ESA program on public school finances, Arizona’s FY 2020 budget enacted an explicit subsidy for the public school system using ESA program savings. Specifically, the state budget directed \$3 million of savings generated by ESAs to begin funding the overhaul of the state’s public school payment system.<sup>31</sup>

These dollars—generated by formula savings and originally set aside for ESA administration—will fund the redevelopment of the Arizona Department of Education’s (ADE) IT system, which is responsible for calculating the payments to every single public school in the state. While critics of the ESA program might shrug off a mere \$3 million contribution, it is

telling that a program serving just a few thousand pupils has generated surplus funds that will now be used to benefit over 1.1 million public school students.

In fact, the previous State Superintendent of Public Instruction had even described replacing the Windows XP-era computer system as the department's "greatest need," warning that "If we really care about protecting the student data of 1.1 million children, we can't allow this [current outdated system] to continue."<sup>32</sup> Despite such warnings, other education spending priorities routinely received greater attention in state budget negotiations, leading to a standstill in the system's redevelopment until this new injection of ESA-generated funds.

### Reality: ESAs' Impact on Individual Districts

Far from gutting Arizona's public school system of available funding, it is clear that ESAs produce a modest indirect financial benefit to it in the aggregate. But what about the individual districts and charter schools losing students—and therefore funding—to the ESA program?

Certainly, district and charter schools alike enjoy a larger budget capacity as they enroll more students and conversely can face financial challenges when their enrollments suddenly decline. Schools face certain fixed costs when it comes to facilities and various other expenditures that may not decrease in lockstep with declining student enrollment. There is undoubtedly merit to these concerns, though as EdChoice researcher Dr. Benjamin Scafidi observed in 2012 in *The Fiscal Effects of School Choice Programs on Public School Districts*:

Lobbyists for public school leadership and their allies routinely argue, "when one student leaves, we still have to pay for that student's teacher. We still have to pay for [x,y, and z]." The

implication of their argument is that all costs of running public schools are fixed. Interestingly, I have never heard that argument made when there is an increase in the number of students. If a public school adds only one student, do the lobbyists for public school leaders suggest that the district should not receive any extra funding?<sup>33</sup>

Indeed, while Scafidi himself agrees that districts face short-term fixed costs, his empirical findings from Georgia public schools "show that it is possible for school districts—large and small—to reduce instructional and support costs more than proportionately in response to a reduction in their student populations," often even over the course of a single year. (He concedes that this logic only applies to 99.66 percent of Georgia's public school population, as "very tiny" districts may have greater difficulty making rapid adjustments. In Arizona, however, extremely small school districts have additional authority to raise as much funding as the local school board deems necessary, so this issue would largely be moot.<sup>34</sup>)

Moreover, Scafidi notes that even a district's remaining short-term fixed costs become variable, since "long-term, it does not need as many school buildings or as many assistant principals," and "new schools do not need to be opened, districts and schools can consolidate, etc."<sup>35</sup> Regarding Scafidi's latter point, Arizona is currently spending over \$110 million per year building new schools.<sup>36</sup>

In other words, districts have the ability to adjust in both the short and long term to accommodate changes in enrollment—which, as shown above, are driven in exceedingly small degree by ESAs.

But perhaps this remains cold comfort to those who still believe that ESAs and other school choice alternatives damage traditional public schools. Contrary

to that narrative, however, ESAs have actually directly benefitted school districts.

## ESAs Benefit Special Needs Families While Easing District Budgets

Though rarely acknowledged by critics of the program, ESAs have relieved budgetary pressures on school districts by serving one of the highest-need, highest-cost student populations in the state: students with severe disabilities. The Arizona School Boards Association (ASBA) has stated that “a growing number of students with more severe disabilities” enrolling in district schools has contributed to “straining general classroom spending in Arizona’s public schools” because the cost to provide federally mandated special education services for these students exceeds the funding they generate under the existing public school finance formula.<sup>37</sup>

ASBA reported that to make up the difference, school districts frequently dip into the money intended to provide classroom resources for other (non-special needs) students. As ASBA’s director of research observed, “Where is that money going to come from? Your general operations, so you’re going to increase class sizes, you hire fewer teachers, and you don’t have raises for teachers.”

In other words, school districts are reportedly pressured to take money from other students’ classroom instruction to meet federal requirements associated with serving each special needs student with a significant disability.

Yet as discussed above, students with major disabilities constitute the single largest group of beneficiaries within Arizona’s ESA program. More than 2,500 of these students participated in FY 2019. Not only did their families receive an average of \$26,707 through the ESA program in FY 2019 to customize a learning environment for them, but also the local school

districts no longer needed to provide a cross-subsidy from other students’ classroom resources to comply with federal regulations in an attempt to serve them.

### Claim: ESAs Harm Taxpayers

*“ESAs don’t save the state money. They actually cost the state more.”*

— Arizona School Boards Association<sup>38</sup>

As described earlier in this report, the average (non-special education, non-kindergarten) ESA award totaled \$6,148 in FY 2019, compared to the \$10,120 average per pupil costs of Arizona public school students statewide. Yet various organizations opposed to ESAs have suggested that ESAs represent a net cost to Arizonans.

This charge does have some merit to it—but only to the extent that a \$1,000 income tax cut coupled with a \$500 property tax increase, for example, would constitute a net cost to a taxpayer.

### ESA Price Tag Sounds High with Spin ...

Due to the way the school finance system is set up, Arizona taxpayers fund traditional district schools by paying local property taxes, state sales and income taxes, and federal taxes.

For ESAs and charter schools, however, taxpayers do not pay local property taxes at all, nor any state taxes to support funding for transportation or facilities (as they do for district school students).

To make up a portion of the forgone funding, charters and ESAs receive greater “additional assistance” support, which is funded exclusively from the state’s General Fund. While critics thus seize on this fact to argue ESAs cost more “state money,” they are conspicuously referring to just a single component of the funding formula while ignoring all other state funds as well as the thousands of dollars of local property





taxes that go into supporting a typical district student on average.<sup>39</sup> (As described above, for example, the Classroom Site Fund provides roughly \$532 of state funding to each district student and \$0 to ESA recipients, yet this disparity is completely ignored.)

ESA critics thus rely on arbitrary distinctions about which taxes should or shouldn't be counted when describing the program's costs versus traditional public education. The Arizona residents who actually pay these taxes would likely be unamused if similarly told to ignore a portion of their tax bill because it first gets routed to a county treasurer rather than the state's Department of Revenue.

### ... Or With Half the Facts

Besides claiming that ESAs cost more state money than traditional public schools, critics routinely cast the program as a hugely expensive side project benefiting only a small number of students.

For example, the *Arizona Republic* reported in 2019 that the "total cost of the [ESA] program is \$80 million to \$82 million this year," yet the paper conspicuously left out all mention of what educating those same students in the public school system would have cost Arizona taxpayers.<sup>40</sup> Especially given the large percentage of students with severe disabilities served by the program, that amount would almost certainly have exceeded \$100 million.<sup>41</sup>

### Claim: ESAs Fraught with Fraud and Abuse

Arizona's ESA program gained national attention this past year amid reports it had given rise to widespread fraud and abuse. For example, *Education Week* reported that "according to a recent audit by the state's attorney general ... Arizona parents fraudulently spent \$700,000 in fiscal 2018 on banned items and services" via the ESA program.<sup>42</sup> A number of colorful examples were cited in which parents had spent ESA funds on items disallowed by state law.



## Reality: ESA Parents Are a Vulnerable Population, not Criminal Masterminds

Unlike the Arizona Auditor General—who has noted that ESA misspending arises from a host of circumstances—media reports like the one above have taken the liberty of attributing the misspending entirely to “fraudulent” activity.<sup>43</sup> In other words, they suggest that ESA parents engaged in \$700,000 of *intentional deceit*.

This narrative quickly erodes when considering that many ESA purchases labeled as “misspending” have been educational in nature and made by parents who believed the expenditures were allowed under the program. In some cases, they were even identical to purchases the Arizona Department of Education had approved in the past.

Perhaps no example illustrates this more starkly than a 2019 episode in which ADE sent several families from the Navajo reservation threats of expulsion from the ESA program, demanding they repay thousands of dollars they had used to send their students to a private school.

ESA statute requires that tuition payments go to schools located within Arizona—and the school in question happened to fall roughly a quarter of a mile outside the Arizona state line in New Mexico—so ADE issued them letters demanding repayment of “misspending,” ignoring the fact the department itself had approved tuition payments to the school in the past and provided no warning of a change in policy to these families.<sup>44</sup>

More broadly, ESA parents have struggled to navigate a complicated set of rules and regulations governing what expenditures are allowed. These rules have not only changed or been applied inconsistently by ADE year over year, but have left parents unsure of when an item is considered allowable as a “curricu-



lum” purchase or disallowed for being “supplemental” to a curriculum, for example.

Certainly bad actors exist in the ESA program, as with any other. But like many patients who have received surprise hospital bills after finding out their healthcare services are not covered by their insurance—like when a hospital is “in-network” but a certain doctor there is not—a great many of these ESA parents would seem poor candidates for condemnation and allegations of fraud.

## Reality: 99 percent of ESA Funds Are Spent as Intended

Reported ESA misspending thus encompasses expenditures that were clearly not fraudulent in nature. Yet there is an even larger problem with the narrative that ESAs are synonymous with abuse of taxpayer dollars.

The reported \$700,000 of misspending in FY 2018 came amid roughly \$60 million flowing to parents through the ESA program in the 2017-2018 school year.<sup>45</sup> This means total misspending amounted to about 1 percent of program funds, with the fraction truly related to fraud being even smaller.

As a comparison, consider another government-administered program that involves a debit card: the

Supplemental Nutrition Assistance Program (SNAP), also known as food stamps. Described by the left-leaning Center on Budget and Policy Priorities as an “effective and efficient” pillar of the social safety net, SNAP accrued \$592.7 million of fraud and mispending in 2016. Coincidentally, that translates to just shy of 1 percent of the program’s total.<sup>46</sup>

Or consider the National School Lunch and Breakfast Programs. As recently observed by Heritage Foundation scholar and Goldwater Institute Senior Fellow Jonathan Butcher, “According to the Office of Management and Budget, the National School Lunch Program lost nearly \$800 million owing to improper payments in fiscal year 2018, while the School Breakfast Program lost \$300 million.”<sup>47</sup> As Butcher observes, “Over the last four years, these programs have had improper payment rates of 16 percent and 23 percent, respectively.”

This is not to suggest the public should ignore the hundreds of millions of dollars of misuse and improper payments taking place in SNAP or other food service arrangements. To the contrary, policymakers should aggressively safeguard taxpayer money. Yet ironically, as Dr. Matthew Ladner of the Arizona Chamber Foundation has pointed out, the very legislation that would have expanded ESA eligibility to all Arizona families in 2018 would also have strengthened the accountability and transparency of the ESA program. For example, it would have required the state to contract with a financial management firm to run the program and mandated ADE to post information on all program expenditures online for maximum transparency. But due to the efforts of the Arizona group Save Our Schools (SOS) and other opponents of parental choice, that measure was defeated—along with the very ESA reforms that would have stemmed misspending and clarified program guidelines for parents.<sup>48</sup>

Thanks to additional efforts by the Arizona Legislature and with cooperation from ADE, the state recently enacted a new requirement that the department contract with a financial management firm to help administer the ESA program. Bringing in a provider with expertise in processing transactions offers parents hope for a streamlined system in which their ESA purchases will be more easily and rapidly verified and approved, hopefully eliminating troubling situations for families before they arise.

## Conclusion: National and State Level Implications

Arizona’s ESA program—like the growing number of education savings accounts across the nation—has offered thousands of students an additional educational pathway best suited to their needs. However, like charter schools and other popular forms of school choice, ESAs have often been cast as wasteful of taxpayer resources and harmful to traditional public schools despite the clear demand for ESAs among families throughout the country.

As explored in this report, the nation’s most established ESA program has actually *benefitted* public schools by redistributing funds back to remaining public school students, directing program savings to public school IT infrastructure, and helping to serve one of the most high-need, high-cost student populations in the state—all while decreasing taxpayer costs and safeguarding public funds.

These impacts—generally unappreciated by pundits and unreported to the public—do not fit neatly with preferred narratives against school choice. They do, however, reflect the realities of school finance in Arizona and offer a case study to other states looking to craft or enhance education savings account programs.

In particular, states looking to establish or improve ESA programs should look to Arizona for a number of key lessons:

- 1) Ensure that education savings accounts reach children most in need of flexibility, such as those with special needs, and those from military families, Native American reservations, or foster care.
- 2) Consider all aspects of available state and local funding to maximize equity between traditional district schools, charter schools, and ESA participants.
- 3) Identify both the educational and fiscal benefits of ESAs to taxpayers and/or public schools as applicable.
- 4) Ensure a streamlined, parent-friendly process for reviewing and approving ESA expenditures:
  - a) Contract with an experienced vendor to manage the financial administration of the program.
  - b) Protect ESA parents against “surprise bills” by requiring the program’s administrative body to notify them of any policy changes before demanding repayment for expenditures that were previously approved.

Finally, while the intricacies of school funding formulas differ from state to state, policymakers across the country should be reminded that much of the funding available for K-12 education remains in the public school system even as students exit for alternatives like ESAs, which leads to higher per pupil funding among remaining public school students.

Those who are skeptical of this claim or unpersuaded by its significance should imagine what their reaction would be if these public school benefits were

eliminated. In Arizona, for example, consider if each student’s Classroom Site Fund dollars began following them from their public school to their ESA, rather than going back to support remaining public school students as the money does now. Or nationally, if proposals for Title I portability succeeded in letting federal funds follow students when they leave a district school, rather than remaining in the public school system as the funds often do now.

In the absence of such proposals, however, both the advocates and opponents of expanding families’ educational options should acknowledge that ESAs provide a net benefit to students, states, and our educational systems at large.

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